Ceylon Electricity Board and Its Subsidiaries - 2013

The audit of financial statements of the Ceylon Electricity Board (CEB) and the consolidated financial statements of the Ceylon Electricity Board and its Subsidiaries for the year ended 31 December 2013 comprising the statement of financial position as at 31 December 2013 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory information was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 13(1) of the Finance Act, No 38 of 1971 and Section 49(4) of the Ceylon Electricity Board Act, No.17 of 1969 as amended by Act, No.31 of 1969. My comments and observations, which I consider should be published with the Annual Report of the Ceylon Electricity Board in terms of Section 14(2) (c) of the Finance Act, appear in this report. The financial statements of the Subsidiaries were audited by the firms of Chartered Accountants in public practice appointed by the Board of Directors of the respective Subsidiaries.

1.2 Responsibility of the Management for Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

1.3 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments the auditor considers internal control relevant to the Board's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. Sub-sections (3) and(4) of Section 13 of the Finance Act, No.38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

1.4 Basis for Qualified Opinion

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

2. Financial Statements

2.1 Qualified Opinion – Board

In my opinion, except for the effects of the matters described in paragraph 2.2.2 of this report, the financial statements give a true and fair view of the financial position of the Ceylon Electricity Board as at 31 December 2013 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

Qualified Opinion – Group

In my opinion, except for the effects of the matters described in paragraphs 2.2 of this report, the consolidated financial statements give a true and fair view of the financial position of the Board and its Subsidiaries as at 31 December 2013 and their financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2 Comments on Financial Statements

2.2.1 Group Financial Statements

The auditors of the Subsidiaries and the Joint Venture of the Board other than the Lanka Coal Company Limited had expressed clear opinion on their financial statements for the year 2013.The Names and the ownership of the Subsidiaries are as follows.

Name of the Subsidiary	Ownership as a Percentage
Lanka Electrical Company (Pvt) Ltd.(LECO)	55.2
LTL Holding (Pvt) Ltd	63
Lanka Coal Company (Pvt) Ltd.(LCC)	60
Sri Lanka Energies (Pvt) Ltd.	100
Trincomalee Power Company Ltd.(Joint Venture)	50

The auditors of Lanka Coal Company (Pvt) Ltd had issued a qualified opinion on the financial statements of the Company for the year ended 31 December 2013 based on the following observations.

(i) Documentary evidences were not provided in the form of direct confirmation to verify the accuracy and existence of the balances of prepayment and creditors amounting to Rs. 1,789,698,174 and Rs.1,792,294,204 respectively as at 31 December 2013.

(ii) Agreed tax liabilities with the Department of Inland Revenue approximately Rs. 100 million had not been brought to the financial statements.

2.2.2 Financial Statements of the Ceylon Electricity Board

2.2.2.1 Sri Lanka Accounting Standards (LKAS) and Accounting Policies

The following observations are made.

(a) **LKAS 2 - Inventories**, According to the Standard, the inventories should be measured at lower of cost or net realizable value and the cost of inventories should be determined by using the First In First Out (FIFO) or Weighted Average Cost formula. But, the Board had used Standard Prices Method for valuing its inventories at the Distribution Regions contrary to the provisions in the Standard.

Further, according to the directions issued by the Institute of Chartered Accountants of Sri Lanka, standard costs would be allowed for inventory valuation where prices are subject to fluctuation, otherwise the value of inventories should be computed at the lower of cost or net realizable value.

The following observations are also made in this regard.

(i) According to the prevailing situation prices had only been increased without being fluctuated. Therefore, it was clear that the Board had overestimated their standard prices of the inventory items than actuals in most instances. For instance, the net income recognized by overestimation of the material prices and labour rates in 2013 was Rs. 3,444 million (2012 – Rs. 1,647 million) and Rs. 1,213 million (2012 – Rs. 1,034 million) respectively. In addition to that a sum of Rs. 1,568 million (2012 – Rs. 1,574 million) had been charged to the cost of the jobs as overheads (computed by applying standard rate for actual labour hours used) which had been recognised as an income in the statement of comprehensive income.

As a result, the values of the stocks, maintenance works, work-in-progress and completed capital jobs shown in the financial statements as at 31 December 2013 had not been fairly reflected.

(ii) Uniform policy for valuing the assets constructed by the Board had not been followed. For instance, the Transmission Lines and certain Distribution Lines constructed out of foreign funded Projects had been valued at actual cost while other jobs such as Service Main Connection (SMC), System Augmentation (SYA), Jobs carried out from Iran funded Projects, Project's works carried out under Gamanaguma and Decentralized Budget (DCB) etc. had been valued at standard cost.

(iii) The impact on the operating result for the year 2010 to 2013 due to valuing the stocks at standard cost was as follows.

Year	**Operating Result as per the Financial Statements with Price Variance**	**Total Net Positive Price Variance**	**Operating Result without the Price Variance**	**Price Variance as a Percentage of Operating Result**
	Rs. million	**Rs. million**	**Rs. million**	**%**
2013	12,846	5,466	7,380	43
2012	(77,645)	2,675	(80,320)	3
2011	(19,266)	4,494	(23,760)	23
2010	4,832	3,295	1,534	68

According to the above analysis, it was revealed that when the profit or loss is larger, the impact due to price variance is smaller and vise-versa.

(b) **SLFRS 05 - Non-current Assets Held for Sale and Discontinued Operation**

Assets that meet the criteria referred in the SLFRS 05 to be classified as held for sale and to be measured at the lower of carrying amount or fair value less cost to sell and presented separately in the statement of financial position. However, the Generation Division and Transmission Division had not complied with this requirements and net book value of 60 vehicles amounting to Rs. 24,565,471 held for disposal had been included in the value of the vehicles shown under the Property Plant and Equipment (PPE) in the statement of financial position as at 31 December 2013.

(c) **LKAS 16 - Property, Plant and Equipment (PPE)**

(i) GT 7 (Fiat Gas Turbine) with a capacity of producing 115 MW electricity installed at Kelanitissa Power Station was commissioned in 1997. The major overhaul of the plant was done after 100,000 equivalent running hours and cost incurred to the overhaul was Rs 793,525,443 and those expenses had been treated as recurrent expenditure. However, according to the nature of the transaction, those overhaul cost will help to increase the future economic benefit of the power plant and therefore, that expenses should be treated as capital expenditure.

(ii) Depreciation is to be calculated based on the major component of the assets. However, Lakwijaya Power Station commissioned in 2011 had been depreciated its power plant considering as a single asset which includes various components such as access roads and infrastructure developments within the premises, power plant, deaf coal, etc. amounting to Rs. 46,083 million without having equal economic useful life.

(iii) Underground cable system (13Kv) included in the fixed assets had been depreciated based on the economic useful life of 12 years since the year 2012. But, according to the stated policy, on these assets should be depreciated based on the economic useful life period of 35 years. Therefore, both property, plant and equipment and the retain profit shown in the financial statements as at 31 December 2013 had been understated by Rs.159,441,901 due to over provision of depreciation during the previous year.

(d) **LKAS 17- Leases**

(i) Lessee shall recognize the finance leases as assets and liabilities in their statement of financial position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments. However, the cost of eight vehicles purchased by Transmission Division in the year 2013 on financial lease basis had not been recognized in the financial statements on that basis. As a result, the property plant and equipment shown in the financial statements as at 31 December 2013 had been understated by Rs.7,087,215.

(ii) Lease interest to be charged to the statement of income using the actuarial method or sum of digit method. However, Transmission Division had charged lease interest equally in every month and as a result, the lease interest and interest in suspense account shown in the financial statements had been understated and overstated by Rs.6,198,720.

(iii) The following overstatements and understatements were observed between the amounts shown in the financial statements and the calculation made by the audit, based on the information furnished.

Item	Amount as per the Financial Statements	Amount as per the Calculation Done by the Audit	Overstatements/ (Understatements)
	Rs.	Rs.	Rs.
Lease Creditor	112,525,344	100,469,040	12,056,304
Interest in Suspense	48,605,344	29,349,065	19,256,279
Lease Interest	12,151,336	16,327,235	(4,175,899)
VAT Portion – Other Expenses	-	3,014,076	(3,014,076)

(e) **LKAS 24 – Related Party Disclosures** - The Board had not disclosed the transactions between the related parties by disclosing the nature of the related party involvement as well as information about the transactions and outstanding balances necessary for understanding the potential effect to the financial statements as required by the Standard. The following contracts granted to the LTL Project (Pvt) Ltd. which has indirect relationship with a Subsidiary of the Board were observed as related party transactions in audit.

(i) Vavuniya Kilinochchi Transmission Line Project – JBIC Funded Project
(ii) Transmission System Strengthening Transmission Line Project - ADB Funded Project
(iii) Transmission System Strengthening Eastern Province Project - ADB Funded Project (Contract amount was Rs. 1,345 million)
(iv) North Eastern Power Transmission Development Project - ADB Funded Project (Contract amount was Rs.425 million)
(v) Augmentation Grid Substation Project Phase II - ADB Funded Project (Contract amount was Rs.1,815 million)
(vi) Augmentation Grid Substation Project Phase I - GOSL Funded Project
(vii) Galle Grid Substation, Augmentation and Rehabilitation Project
(viii) Augmentation of Grid Substation for Absorption of Renewable Energy Project – Augmentation of Seethawaka, Balangoda, Badulla, Nuwara Eliya, Ukuwela Grid Substations and Construction of New Mahiyanganaya Grid Substation (Contract amount was Rs. 2,336 million) (Esot case)

2.2.2.2 **Accounting Deficiencies**

The following accounting deficiencies were observed in audit.

(a) Most of the Transmission Projects are being carried out with the assistant of foreign aids. The cost of those projects had been accounted based on the information obtain from the website of the External Resource Department (ERD) without considering the invoices issued by the Project Manager at the year end. Therefore, the work – in - progress (WIP) and equity capital shown in the financial statements as at 31 December 2013 had been understated by Rs. 139 million and Rs. 111 million respectively while overstating the advance recovery and retention money by Rs. 13 million and Rs. 10 million respectively.

(b) Although, the amount receivable from the Ministry of Power and Energy as at 31 December 2013 in respect of the Lighting for special occasions was a credit balance of Rs.10 million, the actual amount receivable as per the computation made by the audit based on the correspondence available in the relevant file was Rs.14 million. Hence, the other debtors shown in the financial statements had been understated by Rs.24 million.

(c) The Board had computed the fair values of the motor vehicles belonging to some of its Divisions in the year 2011 by discounting the market value prevailed as at 31 December 2012 and as a result, the Valuation Committee recommended market values had not been reflected in the financial statements of the year 2012 which resulted to understate the balance of the motor vehicles shown in the financial statements in the year under review as well by Rs. 396 million.

(d) The value of property plant and equipment transfers among the individual Divisions should be zero in the financial statements of the Board. However, un-reconciled differences aggregating Rs. 1,920 million were observed among the transfers in, transfers out and work-in-progress (WIP) transferred to other Divisions during the year 2013. Due to the above lapse, the property plant and equipment shown in the financial statements had been understated by similar amount.

(e) Reimbursement of import duties and taxes amounting to Rs. 94,294,181 relating to some imported equipment of the power plant brought back by the Aggriko Power Company (pvt) Ltd. from the country due to expiration of the Private Power Purchase (PPP) agreement had been accounted as power purchase cost of the year under review instead of being accounted as other expenditure.

It was further observed that there was no provision in the IPP agreement to make such payment at the time of taking the plant back from the country and it was observed that the payment had been made without proper authority.

(f) The under mentioned items had not been taken into account in determining the cash flows of the year under review and as a result the real cash flows of the Board had not been reflected from the statement of cash flow.

(g) Interest amounting to Rs.7, 818,402 payable to the Ceylon Petroleum Corporation due to delay in settlement of fuel bills relating to the month of July 2013 had not been

Item	**Amount** **Rs.**	**Impact**
Overhead Recoveries (Estimated figures included in the value of the electrification jobs – both capital and maintenance)	1,676,805,270	Overstated the net cash generated from operating activities. However, real impact could not been ascertain due to non-availability of the portion relating to the cost recovery jobs.
Labour Rate Variance	1,213,515,708	Overstated the net cash generated from operating activities
Trade and Other Receivables	561,436,724	Overstated the net cash generated from operating activities
Property, Plant and Equipment	75,626,084	Understated the net cash generated from investing activities
Inventories Receivable	4,979,012,034	Understated the net cash generated from operating activities
Stores Price Variance	3,443,969,186	Overstated the net cash generated from operating activities

brought to the accounts.

(h) Disputed interest payable amounting to Rs. 749,973,935 on delay in settlement of the fuel bills of the Thermal Complex as at 31 December 2013 had not been disclosed in the financial statements as a contingent liability.

(i) Uniform national tariff (UNT) adjustment or bulk supply of electricity to LECO during the period from July to December 2013 amounting to Rs.68 million had been approved by the Public Utility Commission of Sri Lanka (PUCSL) in March 2014. However, the Board had not taken this UNT adjustment into their accounts and as a result, the operating profit as well as the trade debtor balances shown in the financial statements of the year 2013 had been understated by that amount.

2.2.2.3 **Un-reconciled Differences**

The following un-reconciled differences were observed.

(a) The amount due from LECO as at 31 December 2013 as per the financial statements of the Board had not been reconciled with the financial statements of the LECO and a difference of Rs. 86 million was observed between those two financial statements.

(b) Differences of Rs. 45 million, Rs. 68 million and Rs. 22 million were observed in respect of amount due from LECO between the confirmation letter issued by the Board and the amount shown in the financial statements of the Board, and the financial statements of the LECO and the confirmation letter issued by the Board and the computation made by the audit and the financial statements of the Board respectively, for the year 2013.

(c) If the inter Divisional transactions were accounted accurately, there should not be any un-reconciled balances as at end of the year in the Current Accounts of the Board at any given time. However, an un-reconciled inter-current account balance of Rs. 2 million had been shown in the financial statements of the year under review.

2.2.2.4 **Accounts Receivable and Payable**

The following observations are made.

(a) A sum of Rs. 240,939,043 or 65 per cent out of the total debtors balance of Rs. 335,411,224 relating to the Air Condition and Maintenance Unit of the Board as at 31 December 2013 was outstanding for more than 05 years and no actions had been taken to recover such balances in the year 2013 as well.

(b) The Board had not taken adequate actions to recover the trade debtor balances of Rs. 4,095 million even the recoverability period of these balances had been lapsed as at 31 December 2013 enabling the Board to maintain a better liquidity position and proper working capital management throughout the year under review. Further, balance to be received from private sector as compared with the total trade debtor balance of Rs. 21,395 million as at 31 December 2013 was represent 86 per cent.

(c) Other debtor balance of Rs. 2, 280,752,812 remained un-recovered for more than two years as at 31 December 2013. Further, a sum of Rs. 6, 142,277 and Rs. 897,025,999 of them were outstanding from then Ministry of Power and Energy and the Sri Lanka Sustainable Energy Authority respectively. However, this had not been reflected in their accounting records as payable to the Board.

2.2.2.5 **Lack of Evidence for Audit**

The following observations are made.

(a) Title deeds for 12 lands valued at Rs. 38 million owned by the Uva Provincial Office were not made available for audit.

(b) Sub- loan agreements had not been entered into with the General Treasury in respect of 02 loans aggregating Rs. 115,341 million granted by the General Treasury. Further, the repayment schedule and the interest rate on those loans were not made available to audit.

(c) The foreign aid and the capital grant received by the Board for generation, transmission and distribution programmes including rural electrification programmes had been treated as contributed capital for a longer period even though certain such grants had not been considered by the General Treasury as capital contribution. According to the financial statements of the Government of the Democratic Socialist Republic of Sri Lanka for the year 2013, the total capital contribution to the Board was to Rs. 96 billion and according to the financial statements of the Board it was shown as Rs. 122 billion. Accordingly, the accounting treatment made in the financial statements for the difference of Rs.26 billion of Government grant could not be verified due to non-availability of the requisite approvals.

2.2.2.6 **Non-compliance with Laws, Rules, Regulations and Management Decisions etc.**

The following instances of non-compliance were observed in audit.

(a**)** The Board had not submitted a copy of the draft annual report for the year 2013 to the auditor General as prescribed in Section 14(1) of the Finance Act, No. 38 of 1971.

(b) Ceylon Electricity Board Act, No. 17 of 1969

(i) **Section 47 (1)(b)** – The Board may establish and maintain a Sinking Fund with the General Treasury in respect of the repayment of loans taken by the Board. A Loan Redemption Reserve had been shown in the financial statements but it had not been updated since the year 2000. The balance in that Reserve account as at 31 December 2013 was Rs. 17,447 million.

(ii) **Section 47(2)(a) -** The Board may establish and maintain a Depreciation Reserve with the General Treasury to cover the depreciation of the movable and immovable property of the Board. However, in contrary to that requirement, the Board had established a Depreciation Reserve in its financial statements by transferring Rs. 1 million per annum up to 31 December 2000 and thereafter no provision had been made. A sum of Rs. 23 million being accumulated balance on that date had been carried forward in the annual financial statements continuously without any review.

(iii) **Section 47(2)(b) -** The Board may establish and maintain a General Reserve with the General Treasury for the purpose of financing capital works from revenue moneys, ensuring the financial stability of the Board, and for such other purposes as the Board may from time to time determine. However, in contrary to that requirement the Board had established an Other Capital Reserve in its financial statements and it had not been updated since the year 2000. The balance of that Reserve Account as at 31 December 2013 was Rs. 165.45 million.

(c) In contrary to the provisions in Section 46 of the CEB Act, No. 17 of 1969 and Section 11(a) and (b) of Part II of the Finance Act, No. 38 of 1971, the Board had invested its fund amounting to Rs. 5,250 million in the Insurance Escrow Fund as at 31 December 2013 based on the contribution of 0.1 per cent of the total value of the gross fixed assets at the end of each year since 1989.

(d) According to the Financial Regulations 389 and 260, the cheques must be handed over to the person or his representative after verifying the identity. However, 452 cheques valued at Rs. 19,813,345 had been handed over to the persons without complying with the said Financial Regulations.

3. Financial Review

3.1 Financial Results

According to the Board and Group financial statements presented, the operations of the Board and the Group during the year under review had resulted in a pre-tax net profit of Rs. 18,636 million and Rs. 21,500 million respectively as compared with the corresponding pre-tax net loss of Rs. 61,447 million and Rs. 54,607 respectively for the preceding year, thus showing an improvement of Rs. 80,083 million and Rs. 76,107 million respectively in the financial results of the year under review.

As analysed below, the increase of hydro power generation in 2013 by 3,634 GWh or 10 per cent as compared with 3,292 GWh generated in 2012 due to high water level in hydro reservoirs and decrease of expenditure on fuel and power purchase from Independent Power Producer in 2013 by Rs. 12,869 million and Rs. 47,228 million respectively as against the previous year were mainly attributed for this improvement in the financial result of the Board.

Source	Power Generation 2013	Power Generation 2012	Increase/(Decrease)	
	GWh	GWh	GWh	%
Hydro	6,926	3,292	3,634	110
Thermal	4,773	8,339	(3,566)	(42)
Non-conventional Renewable Energy	263	171	92	53
Total	**11,962**	**11,802**	**160**	**1.3**

3.2 **Analytical Financial Review**

According to the information made available, the following table gives the highlights of the financial position as at the end of the year under review and the previous year.

Item	Current Year	Previous Year	Percentage of Change over Previous Year
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	Rs. Million	Rs. Million	
Non-Current Assets	681,014	627,695	8
Current Assets	104,703	107,437	(2)
Total Assets	785,717	735,132	7
Current Liabilities	92,872	137,357	(32)
Working Capital	**11,831**	**(29,920)**	**140**
Total Capital Employed	692,845	597,775	16
Non-Current Liabilities	480,076	406,385	18
Equity	**212,769**	**191,390**	**11**

The following observations are made in this regard.

(a) The total assets of the year under review as compared with the previous year had increased by 7 per cent. Meanwhile, the net current assets had become a positive figure of Rs. 12 billion in 2013 as compared with the negative figure of Rs. 30 billion in the previous year which represented a 140 per cent increase. The main reasons for that increase were repayment of amounts due to CPC and Independent Power Producers (IPP) and the amount so paid in 2013 was Rs. 43,702 million and Rs.78,356 million respectively.

(b) Forty nine per cent of the total capital employed amounting to Rs. 785 billion of the Board as at 31 December 2013 had been financed through borrowed funds whereas the previous year borrowed portion was 68 per cent.

According to the above analysis, it was revealed that the Board had shown a little improvement in its liquidity position in the year 2013 as compared with the previous year.

3.3 Operating Review

The following observations are made.

3.3.1 Direct Cost Analysis

(a) The following table shows a summary of direct cost incurred for the year under review as compared with the previous year.

	2013		**2012**	
	Rs. million	**%**	**Rs. million**	**%**
Fuel	29,425	18	42,515	19
Power Purchase	80,308	48	120,264	54
Coal	10,677	6	11,099	5
Operation and Maintenance	26,196	16	27,530	13
Depreciation	20,319	12	21,011	9
Total	**166,925**	**100**	**222,419**	**100**

According to the above information, it was revealed that 72 per cent and 78 per cent of the total cost for the year 2013 and 2012 respectively was directly related to power purchase and generation.

(b) Even there were enough hydro power generation, incurring of the fixed cost involving with the power purchase agreements was unavoidable and as a result, the Board was unable to achieve one of the most important objective that supplying the electricity at low cost to the general public in the year under review as well. However, the average cost per unit in 2012 was Rs. 23.66 and sold at Rs. 15.56 per unit whereas the unit cost had come down to Rs. 17.70 in 2013 and sold at Rs. 17.93 per unit.

3.3.2 Unit Price Analysis

The following table shows the average (loss)/gain from selling one electricity unit during past five years.

Year	Average Selling Price per kWh	Average Cost per kWh	Gain/(Loss) per Unit
	Rs.	Rs.	Rs.
2013	17.93	17.70	2.22
2012	15.56	23.66	(5.84)
2011	13.22	15.59	(2.37)
2010	13.16	13.02	0.14
2009	13.13	14.71	(1.58)

According to the above table, the current year had recorded the highest gain per unit during last five years.

3.4 Irregular Payments

The following observations are made.

(a) The Board had paid the PAYE tax out of its own funds on behalf of its employees without being recovered from the employees as per the Cabinet Decision taken on 13 December 2007. The PAYE tax paid by the Board overruling said Cabinet Decision as at 31 December 2013 was Rs.1,312 million.

The Chairman of the Board stated as follows in this regards.

Incurring of the PAYE tax by the Board on behalf of the employees has been legalized by incorporated it in the Collective Agreement entered into between the Chairman, General Manager and Trade Unions recently with the concurrence of the Ministry of Power and Energy.

(b) Thirty nine different staff allowances had been paid from time to time to the staff by the Board on the approval of the Board of Directors without obtaining the approval of the Cabinet of Ministers as specified in the Public Enterprises Circular No 95 of 04 June 1994. At the audit test checks it was revealed that such allowances amounting to Rs. 642 million had been paid in the year 2013.

(c) The common lapses observed in respect of reimbursement of 2/3rd interest to the employees for housing loans obtained from external lending agencies are given below. Total amount so reimbursed in 2013 excluding Distribution Divisions was Rs. 1,166 million.

- Employees had been granted loan amount exceeding the eligibility limit
- Interest for personal loans taken by mortgaging properties such as fixed deposits, personal guarantees etc had also been reimbursed
- Loan had been taken by officers jointly with parties other than the spouse
- Produced the informal letters of the financial institutions

- The loans had been taken for settlement of other loans
- The properties relating to the loan obtained were neither the name of the officer nor the spouse

3.5 **Identified Losses**

The following observations are made.

(a) The Puttalam Coal Power Plant had incurred a loss of 1394.33 Mega Watt Hours (MWh) of electricity costing Rs. 25,098 million due to operational failures during the year 2012 and 2013.

(b) According to the Provision in the Financial Regulation 104(1), inquiries should be instituted to ascertain the extent and causes of the loss and to fix the responsibility to the respective parties if an incident of loss occurs and such losses should be reported to the Auditor General as well. However, the loss to the Kukuleganga Power Station due to the incident taken place on 8 June 2013 had not been ascertained and reported to the Auditor General according to the FR and a loss of 1394.33 MWh costing Rs. 25,098 million of the Puttalam Coal Power Plant incurred due to operational failures during the year 2012 and 2013 had also not been reported to the Auditor General.

(c) The value of 35 reported frauds committed in the year 2013 due to weaknesses in the internal control amounted to Rs. 49 million.

(d) The construction activities of the proposed building called "Vidulakpaya" for the Head Office of the Board had been suspended with immediate effect on the decision taken by the Board of Directors. However, the reason/s for that suspense of the construction neither included in that Board decision nor made available to audit. The construction and consultancy cost incurred up to the date of suspense was Rs. 244.15 million.

3.6 **Matters in Contentious Nature**

The following observations are made.

(a) It was observed in audit that the Board had maintained its position in accordance with the Ceylon Electricity Board Act No. 17 of 1969 as amended by Act No.31 of 1969, that the Treasury Circulars and Public Administration Circulars issued by the Government from time to time to maintain uniform procedures and practices in relation to Finance and Administration in all public sector organizations including Public Corporations and Boards are not applicable to them if the Board of Directors of the Board had not allowed to adopt as the administrative rules of the Board. Few such instances are given below.

(i) In contrary to the Public Administration Circular No.15/90 of 09 March 1990 and Public Enterprises Circular No. PED/12 of 02 June 2003, the Board had recruited non-skilled and semi-skilled staff annually as clerks, cashiers, storekeepers, typists, drivers, office aides, labourers etc. without calling for

Island-wide applications from qualified candidates through newspaper advertisements, Gazette notifications etc. as specified in circular instructions. As a result, the Board had lost the opportunity to recruit the most competent persons to the relevant posts.

(ii) Position reported in my previous audit reports regarding the payment of temporary monthly allowance of Rs. 1,000 to the employees of the Board had not been rectified during the year under review as well.

(iii) Instead of granting vehicle loans at 10 per cent to 14 per cent interest as per the Public Enterprises Circular No 130 of 08 March 1998, the Board had granted it at 4.2 per cent interest.

(b) According to the information made available, the Finance Manager of the CEB himself had taken decisions on investment of insurance reserve throughout the past years since 1990 i.e. incorporation of the fund, although the Board had not delegated him the powers for taking such investment decisions. The total amount in the Investment Account as at 31 December 2013 was Rs. 5,250 million.

(c) The shortfall observed between the Insurance Reserve Fund balance and the Investment of Insurance Reserve Fund as at 31 December 2013 amounting to Rs.4,374 million had not been invested as per the self-insurance policy of the Board. There was no proper financial management was in operation in the Board to implement such statutory requirements.

(d) Even though the Board had sold electricity to LECO and purchasing fuel from Ceylon Petroleum Corporation for several years, there are no sales and purchase agreements entered with those two parties.

(d) Any action taken in respect of the followings matters brought to the notice of the Chairman of the Board by my report for the year 2012 was not observed in the year 2013 as well.

- Front cab was replaced with similar unit (24 vehicles)
- A 2T used crane was fixed locally (2 vehicles)
- Original cab was replaced with used cab(2 vehicles)
- Original front cab and rear tray were replaced with used different model cab and tray (1 vehicles)
- Front cab and rear tray were replaced with used units (1 vehicle)
- A crane was fitted locally (1 vehicle)

(f) Capacity charges relating to two sub component namely escalable (covers all administration costs, fixed operational and maintenance fees, and related expenses) and non escalable (debt service obligation of the company) had been paid to the Independent Power Producers (IPPs) in the year 2013. Although the time period for reimbursement of non escalable component (loan reimbursement) had been expired, it was observed that the Board had over-reimbursed that component and the amount so reimbursed in 2013 was US $ 27 million and JPY 183 million **(** in 2012 it was US $ 15 million)**.** The total amount over reimbursed to the IPPs was not made available to audit.

The Chairman of the Board stated as follows in this regard.

It should be noted that the Non-scalable Component does not become zero after the debt service period is over due to components such as Return on Equity and Insurance continue till the end of the Term as indicated in the Tariff/financial templates of the respective Power Purchase Agreement.

(g) The operational and maintenance costs of the power plant owned by the IPPs are included in the escalable cost component of the capacity charges and those costs were paid by the Board ignoring whether they had incurred or not. Further, the taxes relating to the importation of materials and spares for that maintenance were reimbursed by the Board separately. There was no limit for reimbursement of such expenditure.

Further, certain IPPs undertakes maintenance contract of some other IPPs and there were related party and related party transactions among the IPPs. Therefore, prudency of reimbursement of expenditure including taxes without verifying the actual utilization of the imported material for power plants could not be ensured in audit. The total tax so reimbursed in 2013 was Rs. 670 million.

The Chairman of the Board stated as follows in this regards.

Payments for Fixed operational and maintenance costs of the power plant are released to the IPP through the Scalable component of the Capacity Charge on the agreed Tariff as per the PPA. There is no room in the PPA for making the above mentioned payment based on actual costs incurred on the same.

As per the PPA, CEB has to reimburse taxes related to importation of material and spares by the Company for maintenance work of power plant. However, presently there is no such mechanism to physically monitor maintenance work and verify utilization of material being used at the power plant by CEB Staff due to practical difficulties such as limited resources and the necessity of urgent restoration of the power plant. However, Action has been already initiated by CEB to verify the actual utilization of imported materials in the Power Plants on periodical basis.

(h) Four contractors of the foreign funded Projects had purchased 57 vehicles out of the Project funds for Rs. 388,018,653 on behalf of the Project even though there were no such provisions in none of the Project Agreement, the Financial Agreement or the Project Administration Memorandum. Further, all of those 57 vehicles had been registered with the name of the contractors and shown inappropriately in the financial statements as assets of the Project. 17 vehicles out of that had been handed over to the CEB in the year 2013, but no any adjustment had been done in financial statements of the Board.

(i) Even though the CEB has 50 per cent ownership of the Trincomalee Power Company Ltd, a Joint Venture Company, only one directorship out of three had been allocated thereto. Hence, the possibility of making decisions in favour of the other partners is very high.

3.7 Management Inefficiencies

The following observations are made.

(a) The Board had not claimed from the Ceylon Petroleum Corporation for the abnormal shortage of Auto Diesel delivered in the year 2013 and the value of the short supply was Rs. 291,445,480.

(b) According to the Paragraph 7.2 of the Public Enterprises Circular No. PED/12, of 02 June 2003 all public enterprises should have their own Systems/Manuals covering all major operations, regularly revised and updated. However, the Board had not revised and updated its procedure manuals prepared somewhere in 1987.

(c) Loans had been granted to the employees of the Board without any restriction despite of huge financial crisis prevailed during the year under review. The staff loan amount so paid in 2013 for 3,492 employees of the Board other than employees of the Distribution Divisions was Rs. 516 million.

(d) A sum of Rs. 102 million of vehicle loans except motor bicycle loans had been granted to 226 employees of the Board in 2013. The following common weaknesses were observed in this regard.

- Instances of non - producing the documents relating to the loan were observed and as a result, the utilization of the entire loan amount for the intended purposes could not be ensured.
- In most instances, the vehicles purchased from the loan had not been mortgaged to the Board.
- Officers in lower grades (subordinates) had assured for the loans taken by higher grade officers (bosses).
- Instances of granting loans ignoring the eligibility criteria of forty or sixty per cent salary limits of both borrowers and their sureties were observed.
- Loans had been granted to the officers who are in probation period.
- Loans had been granted exceeding the eligibility limits.
- New loan had been granted prior to the completion of five year period of the previous loan.
- New loan had been granted in full by ignoring the settlement of the previous outstanding loan balance.
- Incomplete loan agreements were observed.
- A cheque relating to loan granted for importation of vehicle on custom duty concessionary terms had been drawn on the name of the officer who borrow the loan from the Board instead of the name of

the Bank in which the borrower open the Letter of Credit as per the Circular instructions of the General Manager of the Board.

- Instances of non-checking and obtaining the copies of annual Revenue Licenses and Comprehensive Insurance Certificates in a consistent manner until the full settlement of loans granted by respective divisions were observed.

3.8 Human Recourse Management

The following observations are made.

(a) Scheme of Recruitment (SOR) of the Board had not been updated for a longer period.

(b) One thousand five hundred and seventeen employees had been outsourced by superseding the Board of Directors approved Personnel Plan for the year 2013. The total employees outsourced as at 31 December 2013 was 4,459 which represented 25 per cent of the total staff strength of the Board.

(c) The following essential posts in the approved cadre had been in vacant by 31 December 2013.

Category	Number of Vacant Posts
Executive	174
Middle Level Technical Service	22
Skilled Technical Service	640
Semi- Skilled Technical Service	1,616
Other Skilled Grade	34
Total	**2,486**

(d) The approved cadre for Unskilled Field Service had been exceeded by 1,717.

(e) Seniority is the only factor considered for promotions and no succession plan was made available. Hence, it was observed that the promotion is benefited to the employee but not to the entity. Promotions to key posts are also granted for a very shorter period even less than half a year which reflected a bad practice in the Board.

Further, there was no proper transfer policy or procedures made available at the Board. For instance 52 per cent of the employees of Kolonnnawa Air condition and Maintenance Unit have been working in the same place for 15-37 years.

(f) The Key post in the HR Division is DGM (Personnel) but required HR qualifications and experience for that post had not been specified in the Scheme of Recruitment (SOR) enabling open that post to other services, especially, for electrical engineers. Hence, the existing SOR could not be considered as a completed and accurate one.

(g) The post namely Chief Engineer (HR Policy) in the Personnel Management Section in the Board has been created reflecting mismatch between the two individual professions.

(h) According to the existing SOR, 50 per cent of the total cadre of HRO Service is filled from externally and that percentage is planned to increase year by year gradually up to 85 per cent. However, it was not observed a clear promotion path for those externally recruited employees in the promotion scheme as two engineers covered the head functions in the Personnel Division over a longer period of the Board's history and posts above the class 4 in that Division have been opened to the services other than the field of HR.

Experience required for direct recruitment of HRM and HRO is 06 years in the field of HR in an organization having more than 100 employees which inadequate as compared with the staff strength need to be handled in this organization.

3.9 **Budgetary Control**

Significant variances were observed between the budget and the actuals thus indicating that the budget had not been made use of as an effective instrument of management control.

4. **Systems and Controls**

Deficiencies in systems and controls observed during the course of audit were brought to the notice of the Chairman of the Board from time to time. Special attention is needed in respect of the following areas of control.

(a) Assets Management
(b) Receivables and Payables
(c) Inventory Control and Stock Management
(d) Human Recourses Management
(e) Accounting and Financial Management
(f) Investments and Control over Subsidiaries
(g) Work-in-progress
(h) Project Management
(i) Budgetary Control
(j) Staff Loans
(k) Sales